Supreme Court, U. S.
FILED
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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1973

No. 73-1245

UNITED STATES OF AMERICA, Et Al., - Petitioners

versus

RICHARD V. BISCEGLIA - - - Respondent

RESPONDENT'S REPLY BRIEF

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UNITED STATES OF AMERICA, ET AL., - *Petitioners*

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RICHARD V. BISCEGLIA - - - - *Respondent*

REPLY TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

The respondent replys to the petitioners' writ of certiorari to review the judgment of the United States Court of Appeals for the Sixth Circuit.

COUNTERSTATEMENT OF QUESTION PRESENTED

The government's statement of the question presented is incomplete and therefore misleading because it is not framed within the context of the specific facts and circumstances of this case. A more accurate statement of the question presented, when considered in light of the undisputed facts in this case, is as follows:

> Whether a Special Agent of the Internal Revenue Service has the authority under Section 7602 of the Internal Revenue Code of 1954 to issue a "John Doe" summons against a bank which re-

quired the bank to produce records pertaining to a designated class of transactions which the bank *may* have had with its customers, when the Special Agent admits that the "taxpayer" named in the "John Doe" summons is both an unknown person and ficticious; and that no person or persons is under investigation; and at that time the investigation was, at most, a mere inquiry into a "situation" the government thought was circumspect.

Alternatively, but only in the event that this Court would grant the writ, a second issue is presented, one not decided by the Sixth Circuit, and it is as follows:

> Whether the Section 7602 summons the trial Court ordered to be enforced constituted an unreasonable search under the Fourth Amendment.

COUNTERSTATEMENT OF THE CASE

At the evidentiary hearing below, it was established that Special Agent B. L. Brutscher issued an Internal Revenue summons under Section 7602 on Treasury Department Form 2039 which required the Vice-President of the Commercial Bank of Middlesboro to appear before the Special Agent at a time and place specified therein and to give testimony relating to the tax liability of "John Doe". The wording of that summons in pertinent part is as follows:

> "SUMMONS
>
> In the matter of the tax liability of
> *John Doe*
>
> Internal Revenue District of Louisville
> Period 1970

> The Commissioner of Internal Revenue
> To Richard V. Bisceglia, Executive Vice President, Commercial Bank
>
> At Middlesboro, Kentucky
>
> Greetings: You are hereby summoned and required to appear before B. L. Brutscher an officer of the Internal Revenue Service, *to give testimony relating to the tax liability or the collection of the tax liability of the above named person* for the period designated and to bring with you and produce for examination the following books, records, and papers at the place and time hereinafter set forth:
>
> Those books and records which will provide information as to the person(s) or firm(s) which deposited, redeamed [sic] or otherwise gave to the Commercial Bank $100 bills U. S. Currency which the Commercial Bank sent in two shipments of (200) two hundred each $100 bills to the Cincinnati Branch of the Federal Reserve Bank on or about November 6, 1970 and November 16, 1970." [Emphasis supplied.]

Special Agent Brutscher testified on cross-examination that the "taxpayer" designated as "John Doe" in the 7602 summons was ficticious and that no "taxpayer" by that name either existed or was under investigation.

It was also established at the same evidentiary hearing that certain records of the bank would not disclose or reveal the identity of the person or persons who had made or may have made the exchange of the currency in question. In short, the testimony disclosed that there was probably no way to connect the "situation" which was the subject of the government's inquiry with a bank customer.

Prior to the time this case was actually decided by the Sixth Circuit on appeal, a three-judge panel for the Northern District of California issued an opinion which is of extreme importance in this proceeding. This case was *Stark* v. *Connally,* 347 F. Supp. 1242 (1972), and was concerned with the constitutionality of the Bank Secrecy Act which became effective on July 1, 1972.

This legislation authorized the Secretary of the Treasury to require domestic financial institutions to report any currency transaction involving more than $10,000.00 with any customer. The purpose of those reports were to be used as a surveillance device for the possible detection of wrong-doing on the part of bank customers since the information disclosed by the reporting requirements of the Act had a high degree of usefulness in criminal, tax or other regulatory investigations.

After considering the question of the Act's constitutionality, the three-judge Court in *Stark* held that the reporting requirements required by the Bank Secrecy Act were unconstitutional under the Fourth Amendment. The basis of the Court's opinion was

predicated upon the premise that customers of a bank were entitled to some measure of privacy and that the reporting requirements of the Act violated those rights. Thus, the Court condemned the government's right to survey third party records when a particular person was not under investigation.[1]

The holding in the *Stark* case, which has subsequently been appealed to the Supreme Court (Docket No. 72-1196, argued January 16, 1974) taints the report made by the Federal Reserve Bank to the Internal Revenue Service in the case at bar. If the report required by 31 CFR Section 102.1 admitted to an unreasonable search in contravention of the bank customer's Fourth Amendment rights, then the Internal Revenue Service obtained the information which initiated these proceedings unlawfully, and it is not permitted, therefore, to use such as a lead upon which to predicate the issuance of the administrative summons in this case. [*Katz* v. *United States,* 389 U. S. 347, 19 L. Ed. 2d 576 (1967); *Wong Sun* v. *United States,* 371 U. S. 471, 9 L. Ed. 2d 441 (1963); *Fahy* v. *Connecticut,* 375 U. S. 85, 11 L. Ed. 2d 171 (1963)].

Moreover, the *Stark* disclosure agrees with the conclusion reached by the Sixth Circuit in the case at bar because the Court in *Stark* said that a valid Section 7602 summons may only be issued to secure *relevant* and *material* matter then under inquiry—the correct-

[1]Access to third party records must be relevant and material to the inquiry. Thus, there must be some reasonable relationship between the regulated activity and the public interest. The Court said in *Stark* that no such relationship existed and issued a preliminary injunction against the Secretary of Treasury enjoining him from enforcing the *domestic* reporting provisions of the Act.

ness of a particular taxpayer's return.[2] In short, the requisite tests of relevancy and materiality when predicated and conditioned upon the existence of a particular taxpayer.

The Senate hearings which were held in regard to the Bank Secrecy Act contained pertinent information in regard to established Internal Revenue policy for the issuance of Section 7602 summonses. The relevant portions of those hearings and the official government policy to which we refer will be set out and discussed in detail below.

REASONS WHY THIS WRIT SHOULD BE DENIED

The government is seeking to invoke the jurisdiction of this Court upon one of two alternative grounds. The first predicate is based upon the statement that a conflict in the several Circuit Courts exists as to whether the Internal Revenue Service is authorized to issue a Section 7602 "John Doe" summons when a particular taxpayer is not under investigation. The alternative second ground of the government is based upon the "great importance question". The respondent-bank strongly contends that both of the government's contentions are incorrect.

[2]At page 1249, the Court said:

"Section 7602 et seq., of the Internal Revenue Act of 1954 (26 U.S.C.), already above mentioned, establish procedures whereunder the Secretary of the Treasury, for the limited purpose of ascertaining the correctness of an individual's tax return, may summon the person liable or any person having possession or care of books of account relating to the business of that person or any other person, to appear and to produce such records and to give testimony as may be relevant or material to such inquiry."

I. There Is No Conflict Among the Several Courts of Appeals in Respect to the Issue By the Sixth Circuit in This Case.

The decision of the Sixth Circuit in the case at bar was approvingly cited and followed by the Fifth Circuit in its decision rendered on January 18, 1974, in the case of *United States* v. *Humble Oil & Refining Company,* 488 F. 2d 953, which affirmed a District Court opinion set forth and contained in 346 F. Supp. 944 (1973). Both cases refused to sanction the use of a Section 7602 summons for mere information gathering purposes. The basis for the decision by the Fifth Circuit arose out of facts similar to the ones here. In *Humble Oil* the revenue agent conceded that at the time he issued the summons against the Humble Oil Company that he had not initiated an investigation of any of Humble's lessors, i.e., no particular taxpayer was under investigation when the summons was issued.

The Internal Revenue Service argued in *Humble, supra,* that the scope of a Section 7602 summons must be read in conjunction with Section 7601, which imposed a duty upon the Internal Revenue Service "to canvass and to inquire".[3] The Fifth Circuit challenged the government's position head-on and it was rejected. It said a Section 7602 summons could not be used to canvass and explore third party records when no par-

[3]In rejecting the Internal Revenue Service's position and deciding the case in favor of the Humble Oil Company, the Fifth Circuit said that it confined its opinion to the question of whether the government had exceeded its statutory authority when it issued the summons under Section 7602. This restraint was a self-imposed one and resulted in a refusal by the Court to consider whether the summons was too broad to warrant enforcement.

ticular taxpayer was under investigation. In doing so it approved and followed the rationale of the Sixth Circuit in the following manner [488 F. 2d 962]:

> "* * * In *Bisceglia,* the IRS issued a summons to the vice president of the Commercial Bank of Middlesboro, Kentucky which had deposited $20,000 in one-hundred dollar bills in a Federal Reserve Bank. These bills, being paper thin and apparently held for a long period of storage, were suspected of not having been reported for income tax purposes by the depositors at the Commercial Bank. It was uncontroverted that the IRS neither suspected nor was investigating a particular person or identified taxpayer but merely sought to ascertain first the depositor's identity and only then whether any income tax delinquency had occurred. In maintaining that section 7602 would not support the issuance of the summons, the Sixth Circuit reasoned that:
>
> > 'In this section, Congress has not authorized the IRS to examine records pertaining to the financial affairs of an indefinite number of unspecified persons for the purpose of ascertaining the identity of one or some of those persons who may be taxpayers and liable for taxes.'
>
> *Bisceglia* v. *United States, supra,* 486 F. 2d at 710. We believe that *Mays* and *Bisceglia* constitute the more compelling view."

This conclusion was based in part upon an analysis of the specific language of Sections 7601 and 7602. The Court in *Humble* said that the government was wrong in maintaining that the commissioner's authority under

Section 7602 was coterminous with the power to "canvass and inquire" under Section 7601. In arriving at this conclusion the Court correctly said [488 F. 2d 960]:

> "Our starting point is a comparison of the language contained in the two sections. Section 7601 empowers the Secretary of the Treasury or his delegate to *make inquiries* concerning all persons who may be liable to pay any internal revenue tax. Section 7602, on the other hand, authorizes the IRS to *examine* books and records for the purpose of ascertaining the correctness of any return and the making of a return where none has been filed. The distinction between a section 7601 inquiry and a section 7602 examination, though perhaps elusive when these words are viewed in a vacuum, becomes more salient when one considers first, that the inquiries are to be conducted of 'all persons' while examinations are to be made of 'any person', and second, that the inquiries may occur to the extent the Secretary deems it practicable and from time to time while the examination may occur for the purpose of ascertaining the correctness of any return. The language variances in these two sections amplify the attributes we ascribe to the differing IRS functions contemplated by sections 7601 and 7602 and confirm our observation that the canvass power can be employed rather cavalierly while the summons power can be utilized only when IRS scrutiny of a taxpayer or a group thereof becomes particularized or focused. We agree with the district court that '[t]here must be some nexus between information sought and a specific investigation of specific individuals before

> the government can compel third parties, at their own expense, to give information to the Internal Revenue Service.' *United States* v. *Humble Oil & Refining Company* [73-1 USTC ¶ 9255], 346 F. Supp. 944, 947 (S. D. Tex. 1972). Before a section 7602 summons may issue, the IRS must have traversed the data gathering stage and initiated an investigation."

The Fifth Circuit Court also distinguished, limited, and placed within its proper perspective, the decision of the Seventh Circuit in *Tillotson* v. *Boughner*, 333 F. 2d 515 (1964). First, the Court said that the language in the *Tillotson* case upon which the government relied was dicta. Second, the Fifth Circuit said that the *Tillotson* decision did not give sufficient weight to the language variances between Sections 7602 and 7601. Finally, the Fifth Circuit approvingly followed the basis upon which the Sixth Circuit in the case at bar had distinguished the *Tillotson* decision. The factual differences between *Tillotson* and the case at bar are best summarized from the language in the Sixth Circuit opinion which said [486 F. 2d 712]:

> "We believe, therefore, that *Tillotson* v. *Boughner*, 333 F. 2d 515 (7th Cir.), *cert. denied* 379 U. S. 913 (1964) and the related case of *Schultz* v. *Rayunec*, 350 F. 2d 666 (7th Cir. 1965), cited by the IRS, are inapposite. In those cases, the court ordered enforced section 7602 summonses issued to a third party bank and an attorney during an investigation in which the IRS sought the identity of the person for whom the attorney had obtained a cashier's check for $215,499.95 from the

> bank. The attorney had sent the check to the IRS accompanied by a letter that informed the IRS that the check was for unpaid taxes owed by an anonymous taxpayer. The IRS sought his identity from the attorney, whose claim of attorney-client privilege was upheld in *Tillotson* v. *Boughner*, 350 F. 2d 663 (7th Cir. 1965), and from the bank, which was ordered to disclose the identity of the taxpayer whose money had been used to purchase a cashier's check from it. The court, in the earlier *Tillotson* case, was careful to distinguish the *Mays* case, *supra*, on the ground that in *Tillotson* not only did '*a* taxpayer' exist but also that the bank was requested to assist in determining that 'specific taxpayer's liability.' 333 F. 2d at 516. (Emphasis in opinion). The court did not sanction an examination of bank records pertaining to the affairs of a class of persons when no particular, specific taxpayer was under investigation."

The difference and distinction between the issuance of a Section 7602 summons in conjunction with the government's Tax Preparer Project and the situation in the case at bar are worlds apart.

In those cases where a "John Doe" summons has been sustained against an income tax return preparer, the Internal Revenue Service has first sent an undercover agent posing as a customer to the preparer for the purpose of having an "income tax return" prepared. In each and every instance, of which the respondent is aware, the return which was furnished by the preparer to the undercover agent was incorrect, or the tax preparer had failed to sign the returns as required by Section 6065 of the Internal Revenue Serv-

ice Code. It is of great significance that only *after "setting-up" the preparer* did the Commissioner then seek to secure from the tax preparer a list of his clients in order to determine whether additional sums were due the government by the taxpayer-preparer's customers.

For example, in the case of *United States* v. *Berkowitz,* 488 2d 1235, the Third Circuit distinguished the use of a "John Doe" summons in a Tax Preparer Project case from the situation which is presented in the case at bar. Moreover, the Third Circuit in *Berkowitz* specifically referred to the Bisceglia decision and said that there was no conflict between the respective cases because the facts were different.

The respondent does not agree, therefore, with the government's allegation that a conflict exists among the several circuits on the question presented. The reason for this position is rather straight forward and simple. First the Fifth Circuit in *Humble* specifically approved and followed the Sixth Circuit decision in *Bisceglia.* Moreover, the Third Circuit in *Berkowitz* specifically distinguished *Bisceglia* and said that there was no conflict between the holdings of the two cases. The government has failed then to establish a valid ground for this Court to invoke its jurisdiction to grant the Writ, and the government's asserted jurisdictional prerequisite is obviously not a tenable one.

II. Official Treasury Pronouncements in 1970 Before the Subcommittee On Financial Institutions of the Committee On Banking and Currency of the United States Senate Establish That the Internal Revenue Service Must Have a Particular Taxpayer Under Investigation Before It Is Authorized to Issue a 7602 Summons Against a Third Party and That a Blanket Right to Survey a Bank's Records Was One the Government Confessed It Did Not Possess.

During June of 1970, the Subcommittee on Financial Institutions of the Senate Banking and Currency Committee held hearings in respect to H.R. 15073 and S. 3678 which resulted in the passage of the Bank Secrecy Act, now encoded at 12 USC §1829(b) and 31 USC §§1051-1122.[4] Although this Act has been subsequently held to be unconstitutional by the three-judge District Court in California in the *Stark* case, *supra,* the testimony and prepared statements from Eugene T. Rossides, Assistant Secretary for Enforcement and Operation, Department of Treasury, is instructive from the standpoint of expressing the official traditional view of the scope of a Section 7602 summons.

In reviewing the Administration's proposals in the area of foreign bank secrecy, before the Committee, the Secretary said the Department and the Administration were concerned with three fundamental and competing interests. [Hearings, p. 148].

The first was that the U. S. dollar was and is the principal reserve and financial transaction currency

[4]Hearings on S. 3678 before the Subcommittee on Financial Institutions of the Committee on Banking and Currency, 91st Cong., 2d Sess; at page 147 et seq. (1970).

of the world market and that the dollar's integrity as an international medium of exchange must be maintained. [Hearings, p. 148]

The second was concerned with the government's objective to deter tax evasion by U. S. citizens in the foreign transaction area and to develop proposals that would benefit the collection of revenue. [Hearings, p. 148]

But the Secretary also said that the third basic concern of the Treasury Department in the Administration was to insure and guarantee that the new and enlarged reporting requirements of the Act should be made within the framework and with due regard to this country's traditional and constitutionally guaranteed freedoms. In expressing this concept to the Committee, the Secretary said [Page 149]:

> "Finally, the third basic thought that has been in our minds, and a very important one, is that we have kept firmly in view our traditional freedoms, such as the constitutional prohibition against unreasonable searches and seizures and the right of our citizens to privacy."

Further on in this testimony, the Secretary commented on the domestic and international record keeping requirements of the bills which were before the Committee. He said that the question of access to records in the possession of a third party, in this particular case a bank, had to be governed under the same standards as those which were being used currently on the domestic scene. His explanation of these present

requirements, in this context, in regard to the foreign international disclosure requirements, was as follows [Page 153]:

> "Getting back to international transactions recordkeeping, there are two aspects that I want to stress. You have recordkeeping and then, first, the question of access to the records. *Access to these records would be under the normal legal processes that are in being currently—the various discovery procedures and the protections that are involved with respect to access in regard to a particular taxpayer.*
>
> The other aspect is possible reporting requirements. You can have recordkeeping and access *in a particular taxpayer investigation. The other possibility is to make the taxpayer's banks report all of the transactions to the Government and then the Government can then browse through those records in its own warehouse or office.*" [Emphasis supplied]

The Secretary was unequivocal. He said a "particular taxpayer" must first be under investigation before the government was entitled to have access to third-party records. In the very next paragraph the Secretary said that the proposed Sections 241 and 242 of the Bank Secrecy Act would violate these traditional notions of access to taxpayers' records, and he opposed these provisions and said so in the following manner:

> "This has been under very careful study; it involves one of the key provisions of the bill, sections 241 and 242, *which we oppose, because of*

questions on which we feel quite strongly, unconstitutional searches and seizures, and the right to privacy.

I would like to read that section, Senator, because it is important, and it does—"

After so testifying, the Secretary read from the Administration's prepared statement. Much of the prepared statement is so cogent to the resolution of the jurisdictional aspects of this case, that the liberty is taken to quote from it at length [173-174]:

"If the Internal Revenue Service could survey the foregoing records of international transactions, either by examining them on the premises of the bank or other financial institutions or by requiring information returns as to some of the contents of the records, the usefulness of the records in providing initial leads to cases of possible tax evasion would be enhanced. *Such surveys, however, would extend the utilization of the records beyond their traditional role as a source of information and evidence in an examination of a particular taxpayer.*

The Internal Revenue Code authorizes the Internal Revenue Service to obtain and examine records maintained by banks and others *in connection with the determination of the tax liability of particular taxpayers. There is also a statutory basis for arguing that the Internal Revenue Code authorizes the use of compulsory process for a survery of the records of a financial institution located in the United States. Nevertheless, the Internal Revenue Service has not generally asserted such survey authority, the scope of which has not been reviewed by the courts.*" [Emphasis supplied]

It is very obvious that in the case at bar the Internal Revenue Service has attempted to assert a general survey authority against the respondent-bank's records even though the tax liability of a particular or specific taxpayer was not under investigation when the Special Agent issued the Section 7602 summons. Therefore, it is clear that the government has attempted to, in this proceeding, expand the traditional role of a Section 7602 summons beyond the limits of record access described by the Secretary in his testimony and prepared statement.[5]

Back to the Secretary's prepared statement. Again, the administration refers to the constitutional prohibition against unreasonable searches and seizures and the need to avoid violations of a customer's right to privacy. The Secretary did so with this language [p. 174]:

"We decided against seeking specific statutory authority extending the rights of the Internal Revenue Service to survey the records of international transactions in banks and other financial institutions. In deciding this, we considered the constitutional prohibition against unreasonable searches and seizures and the need to avoid unnecessary incursions against the right of privacy.

[5]It is assumed that the government's "statutory basis" for arguing that the Internal Revenue Code authorizes the use of compulsory process for a survey of records of financial institutions, was based upon its construction of Section 7601 of the Internal Revenue Code which it has presented to this Court in its brief in the case at bar. Of course, this position was soundly rejected by the Sixth Circuit in the case at bar and by the Fifth Circuit in *Humble, supra*, on a very rational and correct basis.

While it is clear that obtaining records by established discovery procedures from the banks and other institutions in connection with the examination of a particular taxpayer would not violate these rights, provision for a survey of such records raises a much more serious questions. We are also concerned that surveys or information returns could have an adverse effect on legitimate foreign investment in the United States. It has been the tradition overseas to place great emphasis on the privacy of financial transactions and a breach of this tradition could adversely affect the flow of foreign funds to the United States.

Balancing these factors, we concluded that it would not be appropriate for us to suggest legislation extending the rights of the Internal Revenue Service to survey the records of banks and other institutions.

Next we considered the approach taken in sections 241 and 242 of S. 3678 and H.R. 15073 which could be used to accomplish the same result by requiring banks and other financial institutions to file information returns setting forth the information contained in the international records. *For the same reasons that we have concluded that we cannot support new legislative authority for the survey of records not tied to a particular taxpayer investigation, we believe it inappropriate to support legislation requiring reports of information obtained from the records of international transactions. Since sections 241 and 242 of the bills authorized such reports, we cannot support their inclusion unless they are substantially amended . . .*" [Emphasis supplied].

It is readily apparent from the foregoing testimony that Special Agent Brutscher was unaware of the official policy of the Treasury Department in respect to the purported right of the Department of Treasury to survey a third party's records when he did not have the particular taxpayer under investigation. The testimony of the Secretary and the official prepared statement of the Administration which was placed in the Committee's report must be taken as expressing a contrary policy position from that which was set forth in the government's petition before this Court. The fact of the matter is that the testimony of the Secretary is much stronger than a mere statement that the traditional role of a 7602 summons has been limited to surveying records when a particular taxpayer is under investigation because in the proceedings before the Senate the Administration specifically said it would not support any new legislative authority which would authorize the government to survey records which were not tied to a particular taxpayer.

Within this context, then, it is manifest that since the government refused to support legislative authorization to survey the records of a third party not tied to a particular taxpayer that they should not be permitted to say now, before this tribunal, that the records they seek here from the Commercial Bank of Middlesboro are within the scope of their authority to request.

It is easy for the government to take inconsistent positions. The respondent contends, however, that

these admissions and statements of official policy before Congress should be considered as reflecting an unbiased evaluation of the scope of a Section 7602 summons. Obviously, it is commonplace that adversaries in a judicial proceeding over-react and overstate their case. When the government's brief before this Court is considered in the context of the foregoing disclosures, before Congress, it is very apparent that the opinion of the Secretary and the Administration upon the traditional scope and role of the Section 7602 summons was made in the environment of attached objectivity, and represents, therefore, the more correct and rational view of the statutes the government seeks to enforce in this proceeding.

Accordingly, this Court should not grant this writ because no conflict exists among the several circuits in respect to this issue and because the policy question in regard to the enforcement of revenue laws has been clearly set forth by the administration before Congress to be a contrary one from that set forth in the government's brief before this Court.

Respectfully submitted,

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March 13, 1974